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The Changed Architecture of the EU's Agricultural Policy in Comparative Perspective: Implications for a Free Trade Agreement with Australia

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Introduction

The developed countries have long supported and protected their agricultural sectors, using an array of policy instruments such as tariffs, export and input subsidies and mechanisms to increase prices paid to farmers. Justifications for this support have included ensuring food security, supporting a sector seen as integral to national development and culture and offsetting the distortions from the agricultural policies of competitor exporters. With increasing concerns about low growth rates, the cost and inefficiencies of industry support and increasing demands from other sectors (such as manufacturing) for international market access, pressure to 'normalise' agricultural policy increased during the late 1970s and 1980s. Normalisation denotes exposing agriculture to market forces, as opposed to treating the sector as 'exceptional' and therefore outside the expectation of market competition imposed on other sectors.

From the mid-1980s, the GATT and then WTO trade negotiation rounds agreements appeared to have established a framework for normalisation, with three key reform goals to reduce:

- the levels of state support directly related to agricultural production;
- the levels of protection from agricultural imports;
- and subsidies of agricultural exports.

European and neo-European countries generally, though often reluctantly, responded to this agenda. They reduced tariff and non-tariff barriers (Table 1A)[i] and 'decoupled' farm support from production (Table 1B)[ii], though approaches and commitments to normalisation have diverged.

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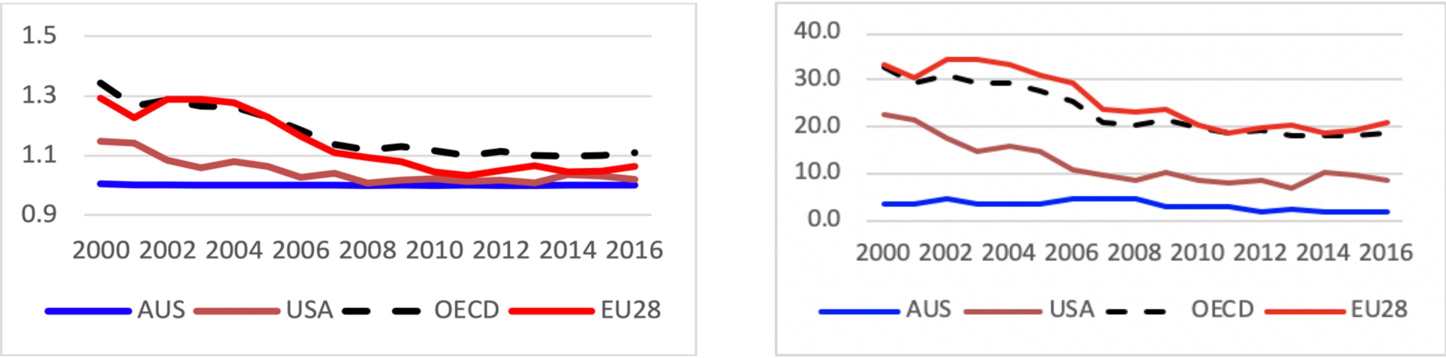
[i] Producer protection, shown in Figure 1A, is defined as the ratio between the average price received by producers (measured at the farm gate), including net payments per unit of current output, and the border price (measured at the farm gate).

[ii] Producer support estimate transfers to agricultural producers, shown in Figure 1B, are measured at the farm gate level and comprise market price support, budgetary payments and the cost of revenue foregone.

Figure 1: OECD Trends in producer protection and agricultural support levels: 2000-2016

A. Producer Production Level B. **Producer support estimate (PSE)**, % of gross



Source: OECD https://data.oecd.org/agrpolicy/producer-protection.htm#indicator-chart and OECD https://data.oecd.org/agrpolicy/agricultural-support.htm#indicator-chart

Australia and New Zealand are mostly holding the line on expecting farmers to be largely self-reliant; the US and Canada have adapted or introduced programs that indirectly link support to production; while the EU is most heavily focused on income diversification, especially payments for landscape services.

The new and evolving programs have allowed the US, Canada and the EU to seemingly settle into levels of support that are politically and fiscally manageable. Furthermore, pressure to make deeper policy retrenchments appears to have receded. There are at least three reasons for this. First, nationalist and mercantilist sentiment is more evident in many nations, including the US. Second, the balance of power within the WTO has shifted from the 1980s when US and EU conflict was a key driver of policy change. Now emerging powers such as Brazil, India and China are more assertive as their economies grow. In particular India and China want to protect and support their agricultural sectors too. Third, bi-lateral and 'regional' trade agreements have displaced negotiations on multi-lateral (WTO) agreements. Hence, WTO negotiations on further agricultural reforms have effectively stalled, leaving nations and blocs considerable latitude in policy development.

The Transformation of the EU's Common Agricultural Policy

In the farm trade negotiations under the GATT's Uruguay Round, running from 1986 to 1994, the EU was under immense pressure to reform its agricultural policy. Eventually, the farm ministers in the EU realised that the Common Agricultural Policy (CAP) had to be reformed to avoid a collapse of the Uruguay Round which included other trade areas in which the EU could potentially achieve significant gains.

Price support was originally the main tool in the CAP to ensure a fair standard of living for the agricultural community. Prices were maintained at a relatively high level within the internal EU market by applying high variable import levies. In combination with the high farm gate prices, significant productivity gains in the European farm sector led to surplus production in the 1970s and 1980s. Therefore, produce had to be removed from the internal market to maintain the politically established minimum prices. This was done by stocking surplus products and exporting with subsidies. The EU's extensive use of export subsidies contributed to driving down world market prices and was the direct cause of trade conflicts.

After a dramatic halt in the Uruguay Round negotiations in late 1990, the EU partially replaced price support with direct farm payments in 1992. Minimum prices were reduced by a third in the arable and red meat sectors. Farmers were compensated for the income loss by direct payments linked to farmed area (on the condition that certain crops were grown and land set aside) and livestock numbers. In the GATT negotiations in the early 1980s, this enabled the EU to commit to reducing export subsidy expenditure by a third and subsidised export volumes by a fifth. The EU variable import levies were transformed into tariffs and on average reduced by 36 per cent and bound.

During the WTO's Doha Round, which commenced in 2001, the EU was again under pressure to reform the CAP and in 2003, most of the direct farm payments were decoupled from the requirement to grow certain crops or keep certain types and numbers of livestock. This meant that the payments no longer required production of certain crops or livestock and would not influence what the farmer would decide to grow. Instead, payments were linked to what became known as cross-compliance, i.e. the farmer is required to comply with environmental, animal health and welfare and food safety regulations to remain eligible for support. The mini-reform of 2008 further decoupled direct payments. The 2013 mini-reform rolled back some of the decoupling adopted in 2008 but the signature change was the introduction of additional environmental measures as a condition for receiving direct farm payments ('greening').

This series of reform means that the CAP is now much less trade distorting than previously. The EU's use of export subsidies has been minimal since 2008, and farm support drives up or maintains production to a much lesser extent. This has lessened the international pressures on the CAP, but tariffs in the red meat, dairy and sugar sectors remain high. Within the EU, these products are considered sensitive. Support measures for these commodities have not fully been aligned with the changes in the arable sectors. The tariffs applied effectively prohibit imports; imports take place only on preferential terms.

Prospects of an FTA between Australia and the EU

As a competitive supplier of sugar, beef and dairy, Australia might aspire to the inclusion of these products in a FTA with the EU. Yet, given the political sensitivity of these commodities within the EU, EU producers can be expected to object to more market access for these commodities. Consequently, one can expect pressure on EU negotiators to maintain high tariffs for these three sectors. According to WTO rules, it is not required that a FTA eliminate *all* trade restrictions; it is sufficient that they are eliminated for 'substantially all' trade.

However, the FTA that the EU agreed with Canada (CETA) indicates that the EU may be willing to give concessions for limited market access for sensitive agricultural commodities. CETA granted increased access for Canadian (hormone free) beef to the EU market in return for protection of EU Geographical Indications (GI) in Canada and increased market access for European cheese. However, with the EU beef sector highly dependent on direct payments and tariffs protection, there is a political limit to such market opening. As former EU Farm Commissioner Cioloş acknowledged shortly after the negotiations with Canada had been concluded, "the EU capacity to absorb additional concessions in the beef sector is limited". He also highlighted the importance of obtaining protection of GIs in return for agricultural market opening in the EU (European Parliament, 2019).

One may wonder why the EU gave the protection of GIs high priority in the negotiations with Canada considering that it is difficult to establish, in general, a significant positive impact of GIs on the rural economy (Török & Moir, 2018) The Irish agricultural economist Alan Matthews argues that they mainly serve a political purpose in the EU's trade policy. As he argues in relation to the unsuccessful negotiations between the EU and the United States on the Transatlantic Trade and Investment Partnership (TTIP)**:**

"Politically, EU agriculture has relatively few offensive interests in the TTIP negotiations so gaining greater protection for foodstuffs as well as wines and spirits GIs is seen as a way to sell a deal to EU farmers as a compensating factor for likely losses for EU livestock producers. Even if the benefits of securing greater GI recognition accrue to relatively few countries and products at the expense of broader EU interests, the absence of a breakthrough on GIs could make a TTIP agreement more difficult to sell to farm groups." (Matthews, 2015)

In the farm trade negotiations between the Australia and EU, the situation is fairly similar: the EU has little to gain and even limited market opening in the sensitive commodity sectors will have to be legitimised in the Council of Agriculture Ministers and not least in the European Parliament to ratify an agreement. In addition to this political importance of the GIs, there may be a belief amongst EU agricultural policy makers that protecting the geographical names is important for rural livelihood. In their book on EU trade policy, Peterson and Young (2014) argue that an overarching feature of EU trade policy is the reluctance of the EU to give concessions on agricultural trade in return for gains in other areas (Young & Peterson, 2014). Protection of GIs, therefore, may be what is needed for the EU to give some concessions on agricultural market opening.

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